



BOULT • CUMMINGS
CONNERS • BERRY PLC

RECEIVED

2003 AUG -4 PM 4:22

Henry Walker
(615) 252-2363
Fax: (615) 252-6363
Email: hwalker@boultcummings.com

August 4, 2003
I.N.A. DOCKET ROOM

Deborah Taylor, Tate Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

Re: *Petition for Arbitration of ITC DeltaCom Communications, Inc. with BellSouth
Telecommunications, Inc. Pursuant to the Telecommunications Act of 1996
Docket No. 03-00119*

Dear Chairman Tate:

Please accept for filing in the above-captioned proceeding the original and fourteen
copies of Direct Testimony of the following on behalf of ITC^DeltaCom:

Joseph Gillan,
Don J. Wood
Mary Conquest
Jerry Watts
Steve Brownworth

I have enclosed an additional copy to be stamped "filed." I appreciate your assistance in
this matter.

Respectfully submitted,

BOULT, CUMMINGS, CONNERS & BERRY, PLC

By: 

Henry Walker
414 Union Street, Suite 1600
P.O. Box 198062
Nashville, Tennessee 37219
(615) 252-2363

HW/pp
Encl.

887962 v1
103062-001
8/4/2003

LAW OFFICES
414 UNION STREET • SUITE 1600 • P.O. BOX 198062 • NASHVILLE • TN • 37219
TELEPHONE 615.244.2582 FACSIMILE 615.252.6380 www.boultcummings.com

**BEFORE THE
TENNESSEE REGULATORY AUTHORITY**

In the Matter of:

**Petition for Arbitration of ITC^DeltaCom
Communications, Inc. with BellSouth
Telecommunications, Inc. Pursuant to
Telecommunications Act of 1996**

§
§
§
§
§
§

Docket No. 03-00119

**DIRECT TESTIMONY OF
JOSEPH GILLAN
ON BEHALF OF
ITC^DELTACOM COMMUNICATIONS, INC.**

Table of Contents

Introduction.....	1
BellSouth Must Offer Local Switching to Serve <u>All</u> Customers	5
BellSouth is Required to Charge "Just and Reasonable" Rates for Switching Subject to the 3-Line Rule	7
Market Rates are Just and Reasonable Only Where There is a Competitive Market	10
The 3-Line Rule Does Not Imply a Competitive Wholesale Market	11
BellSouth's Proposed Rates are Patently Unreasonable and Without Support.....	15
A Just and Reasonable Rate for Local Switching Has Already Been Established by the Authority	16
Recommendation.....	18

August 4, 2003

Introduction

1
2
3 **Q. Please state your name, business address and occupation.**
4

5 A. My name is Joseph Gillan. My business address is P. O. Box 541038, Orlando,
6 Florida 32854. I am an economist with a consulting practice specializing in
7 telecommunications.
8

9 **Q. Please briefly outline your educational background and related experience.**
10

11 A. I am a graduate of the University of Wyoming where I received B.A. and M.A.
12 degrees in economics. From 1980 to 1985, I was on the staff of the Illinois
13 Commerce Commission, where I had responsibility for the policy analysis of
14 issues created by the emergence of competition in regulated markets, in particular
15 the telecommunications industry. While at the Illinois Commission, I served on
16 the staff subcommittee for the NARUC Communications Committee and was
17 appointed to the Research Advisory Council overseeing the National Regulatory
18 Research Institute.
19

20 In 1985, I left the Illinois Commission to join U.S. Switch, a venture firm
21 organized to develop interexchange access networks in partnership with
22 independent local telephone companies. At the end of 1986, I resigned my
23 position of Vice President-Marketing/Strategic Planning to begin a consulting

1 practice. Over the past twenty years, I have provided testimony before more than
2 35 state Commissions (including Tennessee), five state legislatures, the
3 Commerce Committee of the United States Senate, and the Federal/State Joint
4 Board on Separations Reform. I have also prepared reports submitted to the
5 Canadian Radio and Telecommunications Commission and the Finance Ministry
6 of the Cayman Islands. I currently serve on the Advisory Council to New Mexico
7 State University's Center for Regulation and as an instructor at the NARUC
8 Annual Regulatory Studies Program at Michigan State University.
9

10 **Q. On whose behalf are you testifying?**
11

12 A. I am testifying on behalf of ITC^DeltaCom Communications, Inc.
13 ("ITC^DeltaCom").
14

15 **Q. What is the purpose of your testimony?**
16

17 A. The purpose of my testimony is to address Issues No. 26(c) and (d). Specifically:
18

19 c) Is BellSouth required to provide local switching at market rates where
20 BellSouth is not required to provide local switching as a UNE?
21

22 d) What should be the market rate?
23

**Direct Testimony of Joseph Gillan
On Behalf of ITC^DeltaCom
Docket No. 03-00119**

1 As a threshold observation, the way that these issues are framed – in particular,
2 the reference to “market rates” – is misleading. BellSouth is required to charge
3 “just and reasonable” rates for switching, even when it is not a UNE.¹ “Market
4 rates” can be expected to be just and reasonable only where a competitive market
5 exists, which is clearly not the case for local switching in Tennessee today.
6 Consequently, the Authority should reject BellSouth’s so-called “market rates”
7 for unbundled local switching used to serve a customer with more than 3 lines in
8 certain areas of Tennessee (“the 3-Line Rule”).² As I explain below:
9

- 10 1. BellSouth has a continuing obligation to provide ITC^DeltaCom
11 unbundled local switching to serve all customers under section 271 of the
12 federal Telecommunications Act of 1996 (“Act”), whether or not they are
13 also required to offer the network element under section 251.
14
- 15 2. Where BellSouth is not required to offer a network element under section
16 251 of the Act (which, for purposes of this arbitration, are lines subject to
17 the 3-Line Rule), it must still charge rates that are “just and reasonable.”
18
- 19 3. “Market rates” are just and reasonable only when the result of a
20 competitive market. The 3-Line Rule, however, never defined the
21 boundaries of *any* wholesale market, much less a competitive market that
22 could be expected to yield reasonable prices through market interaction.
23
- 24 4. BellSouth’s proposed rates for lines subject to the 3-Line Rule are
25 unreasonable as their face, exceeding cost by 640% (recurring) and

¹ The phrase “even when not a UNE” is intended to refer to situations where a network element is determined by the appropriate regulatory agency to no longer satisfy the “necessary and impair” standard for unbundling under section 251 of the Telecommunications Act of 1996.

² As I explain later in my testimony, the 3-Line Rule was adopted by the FCC in its 1999 UNE Remand decision and excludes certain lines from BellSouth’s unbundling obligation under section 251 of the Act.

1 4,000% (non-recurring). When asked by ITC^DeltaCom to justify such
2 absurd increases, BellSouth's response is that it cannot "locate anyone
3 with knowledge" or "locate any workpapers or documents that may have
4 existed or been used" to determine these prices. Not only should
5 BellSouth be refused approval of these rates on a going-forward basis, but
6 the Authority should also find that BellSouth may not apply these unjust
7 and unreasonable rates in arrears.³
8

- 9 5. There is already an Authority-approved, just and reasonable rate for local
10 switching in Tennessee – the current rate of \$1.89 per port. This rate is
11 now three-years old. The Georgia Commission most recently reviewed
12 BellSouth's switching costs (which are essentially regional, and not state-
13 specific) and determined that the current cost for unbundled local
14 switching is \$0.90 per port. As a result, the existing UNE port rate for
15 unbundled local switching in Tennessee already produces excess margins
16 nearly 100% above cost.
17

18 I recommend that the Authority reject BellSouth's proposed local switching rates
19 (both recurring and non-recurring) for lines subject to the 3-Line Rule with a
20 finding that these prices are unjust and unreasonable (and always have been). The
21 existing UNE rates established by the Authority should remain in effect for all
22 analog switch ports as the only rates that the Authority has determined are just
23 and reasonable to date.⁴ To the extent that BellSouth seeks to impose *different*
24 just and reasonable rates on a particular network element, then it should be
25 required to propose such rates in a separate proceeding (open to all CLECs), fully

³ It is my understanding that BellSouth has only recently developed manual systems capable of billing these charges.

⁴ Section 252(d)(1) of the Telecommunications Act of 1996 requires state commissions to establish rates for unbundled network elements that are "just and reasonable." Therefore, the cost-based UNE rates are defined as just and reasonable rates by the statute.

1 supported by cost and market analysis demonstrating that its proposal is just and
2 reasonable.⁵

3
4 **BellSouth Must Offer Local Switching to Serve All Customers**

5
6 **Q. Please explain how the "3-Line" dispute arose.**

7
8 **A.** BellSouth (like all ILECs) is required to provide competitors access to network
9 elements in accordance with section 251 of the Act when:

10
11 ...the failure to provide access to such network elements would
12 impair the ability of the telecommunications carrier seeking access
13 to provide the services that it seeks to offer."⁶
14

15 In response to a remand by the Supreme Court of its initial interconnection rules,⁷
16 the FCC issued a modified list of network elements that, under certain
17 circumstances, did not include unbundled local switching as a network element
18 under section 251 of the Act. Without debating all the details of the FCC's rule,⁸

⁵ This recommended review process for replacement rates proposed by BellSouth for network elements no longer subject to section 251 should serve as the template for future requests, thereby enabling the Authority to confirm that any such rates are just and reasonable.

⁶ Section 251(d)(2)(B).

⁷ See Third Report and Order and Fourth Further Notice Of Proposed Rulemaking, In the Matter of Implementation of the Local Competition Provision of the Telecommunications Act of 1996, CC Docket No. 96-98, Adopted September 15, 1999, Released November 5, 1999 ("UNE Remand Order").

⁸ Specifically, 47 C.F.R. § 51.319(c)(2), states:

1 the resulting "3-Line Rule" meant that BellSouth was not required to provide
2 local switching to CLECs serving customers with more than 3 lines in the largest
3 central offices in Nashville,⁹ at least under section 251 of the Act.
4

5 **Q. Did the "3-Line Rule" excuse BellSouth from selling unbundled local**
6 **switching to serve these customers?**
7

8 **A.** No. In addition to section 251's *general* obligation on all ILECs to offer network
9 elements satisfying the "impairment" test, Congress imposed very *specific*
10 obligations on the Bell Operating Companies through the competitive checklist in
11 section 271. As part of section 271's competitive checklist, Congress mandated
12 that BellSouth offer: "Local switching unbundled from transport, local loop
13 transmission, or other services."¹⁰

Notwithstanding the incumbent LEC's general duty to unbundle local circuit switching, an incumbent LEC shall not be required to unbundle local circuit switching for requesting telecommunications carriers when the requesting telecommunications carrier serves end-users with four or more voice grade (DS0) equivalents or lines, provided that the incumbent LEC provides nondiscriminatory access to combinations of unbundled loops and transport (also known as the "Enhanced Extended Link") throughout Density Zone 1, and the incumbent LEC's local circuit switches are located in:

- (i) The top 50 Metropolitan Statistical Areas as set forth in Appendix B of the Third Report and Order and Fourth Further Notice of Proposed Rulemaking in CC Docket No. 96-98, and
- (ii) In Density Zone 1, as defined in Sec. 69.123 of this chapter on January 1, 1999.

⁹ There are approximately 135,000 multi-line business lines located in the 15 Nashville wire centers where BellSouth would not have to offer local switching as a network element under section 251 of the Act. This is approximately 20% of all the business lines in the State.

¹⁰ Section 271(c)(2)(B)(vi).

1
2 As a mandatory network element under the competitive checklist, BellSouth has a
3 continuing obligation to offer unbundled local switching to serve *any* customer,
4 irrespective of the number of lines (or other factors). The provision of unbundled
5 local switching to ITC^DeltaCom – including unbundled local switching used to
6 serve customers with more than 3 lines in Nashville – is not some favor granted
7 by a beneficent BellSouth, it is a legal obligation that it must satisfy for it to
8 provide interLATA long distance service in this state.¹¹
9

10 The issue is not whether BellSouth must offer ITC^DeltaCom unbundled local
11 switching to serve all of its customers, the only issue concerns its price.
12

13 **BellSouth is Required to Charge “Just and Reasonable” Rates**
14 **For Switching Subject to the 3-Line Rule**
15

16 **Q. What pricing standard applies to local switching used to serve lines subject**
17 **to the 3-Line Rule?**
18

¹¹ There is no question that BellSouth’s obligation to offer unbundled local switching under the competitive checklist is a distinct obligation to its obligations to offer the network element under section 251 of the Act. As the FCC found in the UNE Remand Order (¶ 468, footnotes omitted):

In this Order, we conclude that circuit switching and shared transport need not be unbundled in certain circumstances. Nonetheless, providing access and interconnection to these elements remains an obligation for BOCs seeking long distance approval.

1 A. The FCC interprets the Act such that the cost-based requirement in section 252 of
2 the 1996 do not presumptively apply to section 271 network elements, unless they
3 are also required by section 251 of the Act (i.e., they satisfy the impair test).¹²
4 Accepting for the moment that the 3-line rule is operative,¹³ then the standard that
5 the FCC adopted is one which requires that the rate be "just and reasonable."
6

7 .If a checklist network element does not satisfy the unbundling
8 standards in section 251(d)(2), the applicable prices, terms and
9 conditions for that element are determined in accordance with
10 sections 201(b) and 202(a).¹⁴
11

¹² This conclusion by the FCC -- i.e., that the mandatory network elements listed in section 271 are not subject to the pricing standard in section 252 -- is highly controversial. The legislative history of the 1996 Act makes clear that Congress understood the competitive checklist to be tied to the section 252 cost-based pricing standard. The Senate Report accompanying the bill setting forth the checklist expressly tied the requirements of section 271 to the section 251/252 process:

 "The Committee does not intend the competitive checklist to be a limitation on the interconnection requirements contained in section 251. Rather, the Committee intends the competitive checklist to set forth what must, at a minimum, be provided by a Bell operating company in any interconnection agreement approved under section 251."

And further:

 "To the extent that a State establishes the rates for specific provisions of an agreement, it must do so according to new section 252(d)."

(S. Rep. 104-23, 104th Cong., 1st Sess. 43, (1995), emphasis added). For purposes of this testimony, I assume that the FCC's interpretation is legally correct, even though I do not agree with the conclusion.

¹³ It is important to understand that the "3-Line Rule" has been remanded to the FCC by DC Circuit Court of Appeals (or, according to BellSouth, vacated). It is expected that the Triennial Review Order, when fully implemented (i.e., at the conclusion of state impairment proceedings), will supplant the 3-Line Rule with a more defensible decision.

¹⁴ UNE Remand Order, ¶470.

Section 201(b) states that “[a]ll charges, practices, classifications, and regulations for and in connection with such communication services, shall be *just and reasonable*, and any such charge, practice, classification, or regulation that is unjust or unreasonable is hereby declared unlawful.” Section 202(a) mandates that “[i]t shall be unlawful for any common carrier to make any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communication service.”¹⁵

Q. Did the FCC reaffirm that section 271 network elements are held to a “just and reasonable” pricing standard when it announced its decision in the Triennial Review?

A. Yes. Although the actual Order had not yet been released, the FCC made clear in the information release when the Order was adopted that the BOCs were required to offer the “mandatory” network elements of section 271 (including local switching) at just and reasonable rates:

Section 271 Issues – The requirements of section 271(c)(2)(B) establish an independent obligation for BOCs to provide access to loops, switching, transport, and signaling, under checklist items 4-6 and 10, regardless of any unbundling analysis under section 251. Where a checklist item is no longer subject to section 251 unbundling, section 252(d)(1) does not operate as the pricing standard. Rather, the pricing of such items is governed by the “just and reasonable” standard established under sections 201 and 202 of the Act.¹⁶

¹⁵ UNE Remand Order, ¶470.

¹⁶ Attachment to FCC Release, CC Docket 01-338, February 20, 2003, page 4.

1
2 There is no ambiguity in these directives – BellSouth must continue to charge just
3 and reasonable rates for any network element required by section 271, even if that
4 network element is not required to be offered by section 251 of the Act.
5

6 **Market Rates are Just and Reasonable**
7 **Only Where There is a Competitive Market**
8

9 **Q. Why does BellSouth claim that it may charge “market rates”?**
10

11 A. BellSouth’s claim reflects an exaggerated reading of the last few sentences of the
12 FCC’s UNE Remand decision where, after several paragraphs explaining that
13 such rates must be “just and reasonable”, the FCC posited that, in *some*
14 *circumstances*, market forces could produce just and reasonable rates. The
15 relevant circumstances, however, would be where:
16

17 ... competitors can acquire switching in the marketplace at a price
18 set by the marketplace. Under these [competitive] circumstances,
19 it would be counterproductive to mandate that the incumbent offers
20 the element at forward-looking prices. Rather, the market price
21 should prevail, as opposed to a regulated rate which, at best, is
22 designed to reflect the pricing of a competitive market.¹⁷
23

24 The above paragraph, however, merely points out that *where* competitive markets
25 exist, that there should be little difference between the “market rate” and the cost-

¹⁷ UNE Remand Order, ¶473. Footnotes omitted.

1 based rate “designed to reflect the pricing of a competitive market.” It is because
2 a competitive market-produced rate and the regulator-established rate would be
3 the same that a “market rate” would be “just and reasonable.”
4

5 The competitive path to reasonable UNE rates, however, is the special case,
6 requiring a wholesale market. As I explain below, there is no evidence to suggest
7 the presence of a competitive wholesale market for switching in Tennessee.
8 BellSouth is not free to establish any price that it wants, unchecked by neither
9 competitive choice nor regulatory review.¹⁸ Because competition cannot be
10 expected to produce just and reasonable rates, the Authority must do so.
11

12 **The 3-Line Rule Does Not Imply a Competitive Wholesale Market**
13

14 **Q. Does the FCC’s 3-Line Rule define a competitive switching market?**
15

16 **A.** No. As I explain below, the FCC lacked a record basis to define relevant markets
17 in its UNE Remand decision, a factor that figured prominently in these rules being
18 remanded on appeal. What little data the FCC did use to develop the 3-Line Rule
19 was not specific to Tennessee, and had *nothing* to do with whether wholesale
20 alternatives were present.
21

¹⁸ Indeed, in a competitive market, BellSouth would be a “price taker,” forced to accept prices determined through market forces.

1 For instance, while the FCC concluded that CLECs required local switching to
2 serve the "mass market," the FCC acknowledged that it lacked the record to
3 define the relevant boundary of the market:
4

5 We conclude that without access to unbundled local circuit
6 switching, requesting carriers are impaired in their ability to serve
7 the mass market.... No party in this proceeding, however,
8 identifies the characteristics that distinguish medium and large
9 business customers from the mass market.¹⁹
10

11 Consequently, even the FCC recognized that it could not design a rule that
12 reflected any reasoned market boundary,²⁰ much less identify the bounds of a
13 competitive wholesale market for local switching.
14

15 **Q. Did the FCC determine that CLECs had wholesale alternatives to the**
16 **incumbent's switches to serve customers with more than 3 lines?**
17

18 A. No. Very much to the contrary, the FCC determined on a national basis that
19 CLECs generally did not have an ability to get local switching from other
20 wholesale providers.
21

¹⁹ See UNE Remand Order ¶291, emphasis added.

²⁰ It is useful to note that the press information released by the FCC when it adopted (but has yet to release) its Triennial Review decision suggests that the boundary between "mass market" and other local switching markets is drawn at the boundary between analog and digital (i.e., DS-1) loops, thereby repudiating the approach underlying the 3-Line Rule that was based on the number of lines.

1 As discussed in detail below, our unbundling analysis focuses upon
2 the ability of a requesting carrier to self-supply switching because
3 the record does not support a finding that requesting carriers, as a
4 general matter, can obtain switching from carriers other than the
5 incumbent LEC.²¹
6

7 The 3-Line Rule cannot be read to imply that CLECs enjoy wholesale alternatives
8 to local switching, when the FCC itself determined that the record supported the
9 opposite conclusion.
10

11 **Q. What was the basis for the 3-Line Rule?**
12

13 **A.** The underlying logic (if that is the correct term) of the 3-Line Rule had two parts.
14 First, the FCC observed that CLECs were self-provisioning switches, generally to
15 serve large business customers. Second, the FCC theorized that if CLECs had
16 access to an Enhanced Extended Loop ("EEL"),²² then self-provided switching
17 could be used to serve larger businesses in the dense urban markets (such as
18 Nashville). Time, however, has shown each of these assumptions to be false.
19

20 As to the viability of self-provided switching, the FCC noted that most carriers
21 self-providing switching were unprofitable, but *assumed* that because such
22 carriers were able to raise capital, the entry strategy must be sound.²³ Capital

²¹ See UNE Remand Order ¶253.

²² An EEL is a combination of a UNE loop and UNE transport that theoretically permits an entrant to extend the reach of its switch to serve customers at distant end-offices.

²³ See UNE Remand Order ¶ 256 (footnotes omitted);

1 markets today are essentially closed to CLECs pursuing this strategy, thoroughly
2 undercutting this assumption underlying the 3-Line Rule. Moreover, EELs have
3 been shown to be economically worthless serving analog customers, with 99.8%
4 of the EELs provided by BellSouth used to serve higher-speed digital customers.²⁴
5

6 The bottom line is that “rationale” used by the FCC when crafting the 3-Line rule
7 provides *no* support for the proposition that CLECs have alternatives to BellSouth
8 switching in Nashville.²⁵ In fact, to the extent the FCC’s analysis is useful at all,
9 it supports the finding that there is *no* competitive wholesale market and,
10 therefore, no basis to expect “market forces” to produce a just and reasonable rate.
11 As I explain below, BellSouth proposed rates leave no doubt that there are no
12 alternatives to its switches in Tennessee.

Indeed, based on financial analysts’ reports of competitive LECs’ operations, a significant number of requesting carriers currently self-provisioning switches are not generating net income (*i.e.*, profits). Thus, it is too early to know whether self-provisioning is economically viable in the long run, although capital markets appear to be supplying requesting carriers with access to capital in the absence of demonstrated profitability.

²⁴ Source: BellSouth Response to AT&T/WCOM 1st Interrogatories, Supplemental Item 2, North Carolina Docket P-100, Sub 133d.

²⁵ The “empirical basis” to the 3-Line Rule is equally suspect, based on a single ex-parte filed by Ameritech on the final day before the record closed (thereby shielding the filing from analysis and response). Notably, during its investigation as to whether the 3-Line Rule should limit competition in Texas, the Texas Commission expressed concern as to the evidentiary validity of the Ameritech submission (Arbitration Award, Docket 24542, April 29, 2002).

BellSouth's Proposed Rates are Patently Unreasonable and Without Support

Q. Do BellSouth's proposed replacement rates for local switching used to serve customers subject to the 3-Line Rule demonstrate that there is no market alternative in Tennessee?

A. Yes. As noted above, a competitive wholesale market should produce rates for unbundled local switching similar (if not equal) to a cost-based rate. Thus, an important criterion in judging the reasonableness of BellSouth's proposed rates is to compare these rates to their underlying cost:

Table 1: Comparing BellSouth Proposal to Cost-Based UNE Rates

Rate Element	Cost-Based Rate	BellSouth Proposal	Mark Up
Recurring Rate	\$1.89	\$14.00	641%
NRC (Existing UNE-P) ²⁶	\$1.03	\$41.50	3,929%

As Table 1 shows, BellSouth's proposed rates demonstrate that alternatives to BellSouth-provided switching do not exist. If there actually were effective market alternatives, BellSouth would not benefit from proposing such massive increases. BellSouth's rates are not "market-based," they are "price them out of the market" based rates.

²⁶ The most relevant NRC comparison is the NRC for unbundled local switching used as part of a combination with the local loop (i.e., UNE-P).

1 **Q. Does BellSouth offer any justification for these prices?**

2

3 **A. No. ITC^DeltaCom specifically asked BellSouth to explain how it developed its**
4 proposed rates. In response, BellSouth claims that it has no information as to how
5 the rates were developed:

6

7 BellSouth has been unable to locate anyone with knowledge or
8 information of the process used to arrive at the “market rate” of
9 \$14.00.

10

11 BellSouth has been unable to locate any workpapers or documents
12 that may have existed or been used by the individuals who
13 developed the \$14.00 market rate.²⁷

14

15 Without passing judgment on the plausibility of BellSouth’s response, there can
16 be no question that the rates themselves are unreasonable, and that BellSouth is
17 unable (or unwilling) to offer any support in their defense.

18

19 **A Just and Reasonable Local Switching Rate**
20 **Has Already Been Established by the Authority**

21

22 **Q. Has the Authority already established a just and reasonable rate for**
23 **unbundled local switching in Tennessee?**

24

²⁷ BellSouth Response to ITC^DeltaCom’s 1st Interrogatories, Items 47 and 48, attached as Exhibit JPG-1. Emphasis added.

1 A. Yes. The existing UNE rates for local switching have already been found by the
2 Authority to be "just and reasonable." The Commission has determined that these
3 rates comply with section 252(d) of the Act, and that section requires that the
4 rates for network elements be "just and reasonable." Consequently, the existing
5 UNE rates already satisfy the fundamental requirement that they be just and
6 reasonable.

7
8 Q. Is there evidence to suggest that the existing rates are likely to be above cost-
9 based levels?

10
11 A. Yes. The existing UNE rates for local switching in Tennessee are now several
12 years old, having been established in March, 2001. BellSouth's switching costs
13 are essentially regional (not state-specific), and have been estimated most recently
14 by the Georgia Commission. The following table compares the local switching
15 rates currently in effect in Tennessee to their Georgia counterpart:

16 **Table 2: Comparing TN Port Rates to the More Recent GA Rates**
17

Port Type ²⁸	Tennessee (March. 2001)	Georgia (March 2003)	Excess ²⁹ Margin
UNE-P Port	\$1.89	\$0.90	110%
Stand-Alone Port	\$1.89	\$1.09	73%

18
²⁸ In more recent cost proceedings, BellSouth typically proposes a different port rate depending upon whether the port is purchased as a "stand alone" UNE or as part of a UNE-P combination (i.e., purchased in combination with an unbundled local loop).

²⁹ It is important to remember that the cost-based rates already include return and a contribution to BellSouth's joint and common costs.

1 As the above table indicates, there is evidence to suggest that the existing UNE
2 rates in Tennessee already exceed (or at the higher end of the range of) the just
3 and reasonable requirements of the Telecom Act. There is no reason to permit
4 BellSouth to charge "just and reasonable" rates higher than these already in effect.
5

6 **Recommendation**
7

8 **Q. What do you recommend?**
9

10 **A.** As I explained above, BellSouth is required to charge a just and reasonable rate
11 for unbundled local switching, even where switching is not required to be
12 unbundled under section 251 of the Act (which, with respect to this arbitration,
13 means lines in Nashville subject to the 3-Line Rule). The rates that BellSouth has
14 proposed are clearly *not* just and reasonable – indeed, BellSouth cannot produce a
15 single document or person that can explain how the rates were even developed.
16

17 While a competitive market could produce a "market" rate that is just and
18 reasonable, no competitive wholesale market for unbundled local switching exists
19 in Tennessee – a fact amply demonstrated by the wildly inflated rates proposed by
20 BellSouth. Moreover, there is no rational reason to even *expect* that a market
21 would develop that conformed to the FCC's "3 Line Rule," which was adopted by

1 the FCC without meaningful evidentiary support (and ultimately rejected by the
2 DC Circuit).³⁰
3

4 **Q. How should the Authority proceed to adopt a just and reasonable rate for**
5 **local switching subject to the 3-Line Rule?**
6

7 A. As noted above, it is important to appreciate that the Authority has *already*
8 established a just and reasonable rate for unbundled local switching when it
9 adopted UNE rates. The relevant issue is whether a *different* just and reasonable
10 rate is appropriate for local switching subject to the 3-Line Rule. On this issue, a
11 couple of points bear repeating.
12

13 First, there is a substantial likelihood that the Authority's existing UNE port rates
14 already exceed (or, at the least, reside at the upper bound of) just and reasonable
15 levels. Second, there is no evidence – and, by this, I mean no evidence, and not
16 just no proof – that wholesale alternatives to serve 4 line customers exist, or are
17 any different than alternative available to serving customers with 3 lines or less
18 (which are none).
19

20 Collectively, these facts mean that the just and reasonable rate should be the same
21 for both groups, because there is no reasoned basis to discriminate between them.
22 Thus, the Authority should require that the existing just and reasonable switching

³⁰ United States Telecom Association, et al. v FCC, 290 F.3d 415 (May 24, 2002).

1 rates (i.e., the UNE rates established in October 2001) should apply to both
2 categories of lines.³¹ If, at some point in the future, BellSouth desires to propose
3 a *different* rate for a network element subject to 271 of the Act (or required to be
4 unbundled by the Authority under state law),³² then it should file a proposed rate
5 with the Authority, in a separate proceeding, fully supported by evidence
6 demonstrating that it is just and reasonable.³³

7
8 **Q. What types of information should BellSouth provide to demonstrate that a**
9 **proposed rate is just and reasonable?**

10
11 **A.** BellSouth should be required to supply information in (at least) two categories:
12 (1) information explaining the relationship between the proposed price and its
13 cost, and (2) information identifying competitive alternatives and how the
14 proposed price compares to the prices charged those alternatives.

15
16 As to the first category of information, the only difference between a cost-based
17 UNE rate (under section 252) and a just and reasonable rate is the level of

³¹ The Authority should also find that BellSouth may not apply its unjust and unreasonable rates in arrears.

³² Although I have not discussed the issue in this testimony, Tennessee law would permit additional unbundling (i.e., beyond the federal minimums) without an impairment finding. *See* T.C.A., 65-4-124(a).

³³ This procedure should generally apply to the pricing of any network element that is no longer subject to the unbundling requirements of section 251, but which still be offered by BellSouth under section 271 of the Act or state law.

1 contribution/profit recovered by the rate.³⁴ The underlying *cost*-basis should be
2 the same, whether the element is required by section 251 or 271. The TELRIC
3 pricing standard establishes the rate for a network element at its forward-looking,
4 average cost.³⁵ Because a competitive market should produce network element
5 prices based on marginal or incremental costs (as opposed to average total costs),
6 comparing margins calculated using TELRIC already include contribution and
7 provide a return. Moreover, by maintaining the same cost-basis, the Authority
8 can focus its review on whether the additional profit sought by BellSouth is just
9 and reasonable.

10
11 As to the second broad category of information, BellSouth should be required to
12 demonstrate that its proposed prices are consistent with the pricing of alternatives.
13 Necessary information would include a listing of the specific competitors that
14 BellSouth claims offer a wholesale alternative to its unbundled local switching (or
15 whatever element it seeks to impose non-UNE prices upon), as well as the prices
16 charged by those competitors.
17

³⁴ I do not intend to provoke a debate about whether the margin (about cost) in a particular proposed price is "profit" or "contribution" to BellSouth's joint and common costs. Whatever BellSouth feels most comfortable *calling* that margin, the important point is that information be *available* for review.

³⁵ The "TELRIC" abbreviation is something of a misnomer. Although the label implies an "incremental" costing methodology, its assignment of joint and common costs necessary to operate and manage a "network element company" effectively means that the cost standard is the average total cost of offering network elements.

1 Another benchmark to determine the reasonableness of a BellSouth proposed rate
2 would be to compare the retail-to-wholesale rate relationship sought by BellSouth
3 to the retail-to-wholesale price relationship in a part of the market where
4 competitive forces do produce "market rates." Specifically, the Authority should
5 review the retail-to-wholesale relationship of BellSouth's long distance services.
6 To provide long distance service, BellSouth leases a combination of "wholesale
7 long distance network elements." This comparison of retail-to-wholesale long
8 distance prices would provide a useful context to judge the relationship between
9 retail-to-wholesale UNE prices in the local market.
10

11 **Q. Does this conclude your direct testimony?**
12

13 **A. Yes.**

BellSouth Telecommunications, Inc.
Tennessee Regulatory Authority
Docket No. 03-00119
Supplement to ITC^DeltaCom's
First Set of Interrogatories
June 12, 2003
Item No. 47
Page 1 of 1

REQUEST: Describe the process used by BellSouth to arrive at the "market rate" of \$14.00 (the recurring charge for a port labeled as "market rate").

RESPONSE: BellSouth has been unable to locate anyone with knowledge or information of the process used to arrive at the "market rate" of \$14.00. The individuals that were involved in the process are no longer employees of the company.

BellSouth Telecommunications, Inc.
Tennessee Regulatory Authority
Docket No. 03-00119
Supplement to ITC^DeltaCom's
First Set of Interrogatories
June 12, 2003
Item No. 48
Page 1 of 1

REQUEST: Identify the business analysis or cost studies undertaken by BellSouth perform to develop its proposed market rates.

RESPONSE: See BellSouth's response to Item No. 47. BellSouth has been unable to locate any workpapers or documents that may have existed or been used by the individuals who developed the \$14.00 market rate.